

**MUNICIPALITY OF SALEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012**

This section of Salem City's annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year ending December 31, 2012. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- During the year, the City's revenues generated from taxes, charges for services, and other revenues for the governmental programs were \$330,112 more than the \$772,796 governmental expenditures. This is an 18.75% decrease over the prior year when revenues exceeded expenditures by \$406,269.
- In the City's business-type activities, revenues increased 7.32% to \$508,380 (this does not include the transfer from the General Fund to pay off the 2003 Drinking Water Bond) and expenses increased 2.65%.
- The total cost of the City's Governmental programs was \$134,107 more than 2011 - up (21%). There were many variables for this increase and are explained in detail on page 7 of this report.
- The revenues for the governmental activities show an increase of 5.55% or \$57,950. The increase in revenue is largely due to an increase in tax revenue. The result of the increase of revenues, increase in expenditures and transfer of dollars to the Water Dept is a \$293,020 increase to Net Assets.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of three parts - management's discussion and analysis (this section), the basic financial statements, including related notes, and required supplementary information. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.
 1. The governmental funds statements tell how general government services like public safety were financed in the short-term as well as what remains for future spending.
 2. Proprietary fund statements offer short- and long-term financial information about the activities that the City operates like businesses. The City has two proprietary funds - the Water Fund and the Sewer Fund.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Figure A-1 summarizes the major features of the City's financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of the overview section of the management's discussion and analysis explains the structure and contents of each of the statements.

Figure A-1
Mayor Features of City of Salem's Government-wide and Fund Financial Statements

	Government-Wide	Fund Statements	
	Statements	Governmental Funds	Proprietary Funds
Scope	Entire City government	The activities of the City that are not proprietary or fiduciary, such as finance office, police, streets, park	Activities the City operates similar to private businesses, the water and sewer systems.
Required Financial Statements	*Statement of Net Assets * Statement of Activities	*Balance Sheet *Statement of Revenues, Expenditures and Changes in Fund Balances	* Balance Sheet *Statement of Revenues, Expenditures and Changes in Net Assets * Statement of Cash Flows
Type of Asset/Liability Information	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of Asset/Liability Information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter no capital assets included.	All assets and liabilities, both financial and capital, and short-term and long-term
Type of Inflow/Outflow Information	All revenues and expenses during year, regardless of when cash is received or paid.	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid.

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the City’s net assets and how they have changed. Net assets – the difference between the City’s assets and liabilities – are one way to measure the City’s financial health or position.

- Increases or decreases in the City’s net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional non-financial factors such as changes in the City’s property tax base and changes in the sales tax revenue base.

The government-wide financial statements of the City are reported in three categories:

- Governmental Activities -- This category includes most of the City's basic services, such as police, fire, public works, parks department and general administration. Property taxes, sales taxes, charges for services, state and federal grants and interest earnings finance most of these activities.
- Business-type Activities -- The City charges a fee to customers to help cover the costs of certain services it provides. The City's water and sewer systems are included here.
- Component Units -- The City includes one other entity in its report - the Housing and Redevelopment Commission. Although legally separate, this "component unit" is important because the City is financially accountable for them.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant funds - not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes.

- State Law requires some of the funds.
- The City Council establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has two kinds of funds:

- Governmental Funds - Most of the City's basic services are included in the governmental funds, which focus on (1) cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at the year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information on the subsequent page that explains the relationship (or differences) between them.
- Proprietary Funds - Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both short- and long-term financial information. The City's enterprise funds (one type of proprietary fund) are the same as its business-type activities, but provide more detail and additional information, such as cash flows.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Assets

The City's combined net assets increased by 8.0% between FY2011 and FY2012; a \$441,586 increase (See Table A-1).

TABLE A-1 CITY OF SALEM NET ASSETS - FISCAL YEAR 2012

	Governmental			Business-Type			Total		
	Activities			Activities			Total		
	2010	2011	2012	2010	2011	2012	2009	2010	2012
Current and Other Assets	1,016,400	1,467,646	1,596,142	602,858	680,917	791,946	1,619,257	2,148,563	2,388,088
Capital Assets	1,755,052	1,701,172	1,880,462	4,171,672	4,083,991	3,998,987	5,926,724	5,785,163	5,879,449
Total Assets	2,771,452	3,168,818	3,476,604	4,774,530	4,764,908	4,790,933	7,545,981	7,933,726	8,267,537
LT Debt Outstanding	11,710	11,138	13,118	2,361,458	2,269,737	2,150,432	2,373,168	2,280,874	2,163,550
Deferred Rev. (salestax)	33,700	40,400	41,200				33,700	40,400	41,200
Other Liabilities	40,437	25,407	37,392	45,536	40,585	37,350	85,973	65,993	74,742
Total Liabilities	85,847	76,945	91,710	2,406,994	2,310,322	2,187,782	2,492,841	2,387,267	2,279,492
Net Assets:									
Invested in Capital Assets									
Net of Related Debt	1,755,052	1,701,172	1,880,462	1,814,424	1,819,654	1,854,542	3,569,476	3,520,826	3,735,004
Restricted	187,933	616,157	633,334	154,597	162,079	170,172	342,529	778,236	803,506
Unrestricted	742,620	774,545	871,098	398,516	472,853	578,437	1,141,135	1,247,398	1,449,535
Total Net Assets	2,685,605	3,091,874	3,384,894	2,367,536	2,454,585	2,603,151	5,053,141	5,546,459	5,988,045
Beginning Net Assets	2,463,949	2,685,605	3,091,874	2,271,178	2,367,536	2,454,585	4,735,127	5,053,141	5,546,459
Increase (Decrease) in									
Net Assets	221,656	406,269	293,020	96,358	87,050	148,566	318,014	493,319	441,586
Percentage of Increase									
(Decrease) in Net Assets	9.0%	15.1%	9.5%	4.2%	3.7%	6.1%	6.7%	9.8%	8.0%

This section explains the differences between the current and prior years' assets, liabilities, and changes in net assets.

The city as a whole reports an increase in net assets of 8%. The Current Assets (cash & receivables) increased 11.1% or \$239,525. The increase of tax revenue and a flat fee rate increase in both the Water & Sewer departments are the main reasons for the increase. The 2012 Street Project and other small projects, less depreciation, resulted in a 1.6% increase in Capital Assets. Total Assets Increased 4.2% Liabilities for the city decreased 4.5%.

There are three categories of Net Assets reported in Table A-1. Invested in Capital Assets Net of Related Debt, Net Assets Restricted and Net Assets Unrestricted.

- The Capital Assets Net of Related Debt increased \$214,178 or 6.08%. The addition of Capital Assets was more than depreciation. No additional debt was incurred and the 2003 DWSRF loan was paid off in January 2012.
- The Restricted Net Assets increased 3.2%. The amount collected in fees exceeded the dollars spent on projects in 2012.

- The Unrestricted Net Assets increased 16.2%. Additional revenue was received from the flat fee rate increases and taxes in 2012.

The Statement of Net Assets reports all financial and capital resources. The statement presents the assets and liabilities in order of relative liquidity. The liabilities with average maturities greater than one year are reported in two components – the amount due within one year and the amount due in more than one year. The long-term liabilities of the city, consisting of compensated absences payable and State Revolving Loans have been reported in this manner on the Statement of Net Assets. The difference between the city’s assets and liabilities is its net assets.

REVENUE COMPARISON, TABLE A-2; FIGURE A-2

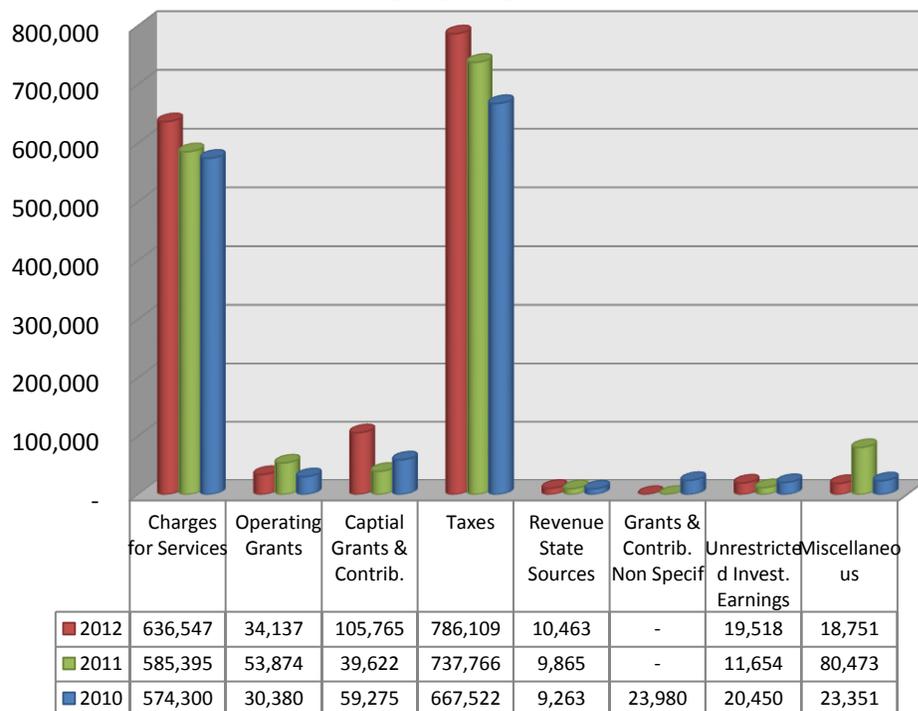
TABLE A-2
MUNICIPALITY OF SALEM
Changes in Net Assets 12/31/2012

	Governmental			Business-Type			Total		
	Activities			Activities					
	2010	2011	2012	2010	2011	2012	2010	2011	2012
Revenues									
Program Revenues									
Charges for Services	129,031	122,685	142,422	445,270	462,710	494,125	574,300	585,395	636,547
Operating Grants	30,380	53,874	34,137				30,380	53,874	34,137
Capital Grants & Contrib.	55,635	39,622	105,765	3,639	-	-	59,275	39,622	105,765
Taxes	667,522	737,766	786,109				667,522	737,766	786,109
Revenue State Sources	9,263	9,865	10,463				9,263	9,865	10,463
Grants & Contrib. Non Specif			-	23,980	-	-	23,980	-	-
Unrestricted Invest. Earnings	12,980	7,324	12,635	7,469	4,330	6,883	20,450	11,654	19,518
Miscellaneous	17,351	73,823	11,379	6,000	6,650	7,372	23,351	80,473	18,751
Total Revenues	922,162	1,044,958	1,102,908	486,358	473,690	508,380	1,408,521	1,518,649	1,611,288
Expenses									
General Government	147,532	147,665	153,493				147,532	147,665	153,493
Public Safety	116,106	92,691	104,104				116,106	92,691	104,104
Public Works	248,820	188,402	310,592				248,820	188,402	310,592
Health & Welfare	4,377	6,448	2,836				4,377	6,448	2,836
Culture & Recreation	178,045	184,627	193,224				178,045	184,627	193,224
Conservation & Development	5,626	16,635	8,547				5,626	16,635	8,547
Miscellaneous Expenditures	(0)	2,221	-				(0)	2,221	-
Debt Service	-	-	-				-	-	-
Water Services				291,010	287,730	296,672	291,010	287,730	296,672
Sewer Services				98,990	98,910	100,234	98,990	98,910	100,234
Total Expenses	700,506	638,689	772,796	390,000	386,641	396,906	1,090,506	1,025,330	1,169,702
Excess (Deficiency) Before									
Special and Transfers	221,656	406,269	330,112	96,358	87,050	111,474	318,014	493,319	441,586
Special Items	-	-	-	-	-	-	-	-	-
Transfers			(37,092)			37,092			
Increase (Decrease) in Net Assets	221,656	406,269	293,020	96,358	87,050	148,566	318,014	493,319	441,586
Ending Net Assets	2,685,605	3,091,874	3,384,894	2,367,536	2,454,586	2,603,151	5,053,141	5,546,460	5,988,045

The City's total 2012 revenues were \$1,611,288 which is an increase from FY2011 of 6.1% or \$92,639.

- Charges for Goods and Services increased 8.7% (Business Type activities increased 6.8% and the Governmental Activities increased 16.1%). The user fees in the Business-Type activities increased as a result of a Water and Sewer rate increases; the General Fund's increase is from a reduction in the garbage hauling contract; a dollar rate decrease was passed onto the residents and the remaining money collected was used to fix streets.
- Operating grants decreased 36.6% as an EECBG grant was received in 2011 to replace the lights in the armory.
- Capital Grants & Contributions increased by 166.9%. Governmental Activities saw the increase from the donation of the cold storage building by the SD National Guards with a fair market value of \$50,000.
- Taxes increased by \$48,343 this reflects an increase in sales tax & property tax revenues. The sales tax revenue increased 8.6% and the property taxes increased 4.6%.
- Revenue from State Sources saw a 6% increase \$598 - these dollars are from Liquor Tax Reversion, Bank Franchise, Motor Vehicle Licenses, Hwy Bridge Funds & County Wheel taxes.
- Grants & Contributions Non Specific - had a zero balance in 2011 & 2012.
- Investment earnings show a 67.5% increase in revenue. The interest rates stabilized and the cash on hand invested was higher than in 2011.
- Miscellaneous revenues decreased 76.7% - (\$61,722). The City sold the bar building in 2011 for a gain of \$65,936. Other misc. revenue fluctuated slightly (cable franchise, dividends and recovery of prior year expenses) showing a \$463.38 increase. Business activities show an increase as dollars were received for the insurance claim on the Water Treatment Plant failure in June 2012.

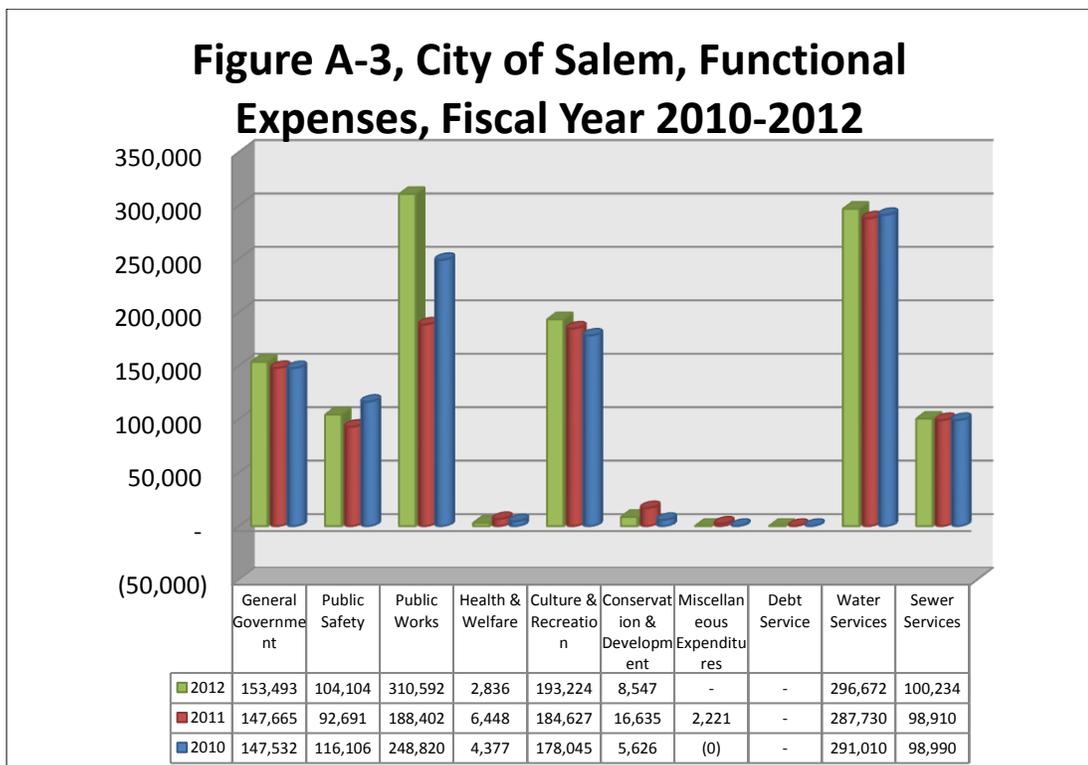
**Figure A-2, City of Salem Revenue Comparison
2010-2012**



EXPENDITURE COMPARISON, TABLE A-2 & FIGURE A-3

The city's expenses show an overall 14.1% increase (2012 vs. 2011).

- General Government Expenditures increased 3.9% or \$5,828. City Hall/Govmt Bldgs saw a significant decrease due to the elimination of the bar building. Administration saw the largest increase as a bi-annual audit was performed in 2012.
- Public Safety increased 12.3%. The police contract remained the same. The fire hall's roof was in need of re-shingling (a metal roof was put on instead).
- Public Works expenses increased 64.9%. In 2012, \$132,366 dollars were spent on street patching, overlays & chip/seal compared to \$32,632 in 2011. Also in 2012, \$11,684 was spent on cleaning out the storm sewer drainage ditches throughout town.
- Health & Welfare expenses decreased 56% - (\$3,612). The dry weather resulted in less mosquito spraying; therefore, fewer chemicals were purchased.
- Culture & Recreation expenses increased \$8, 597 or 4.7%. Summer Recreation costs decreased \$3,220.72; Parks increased \$1,641.91; Auditorium costs increased \$8,615.62. Recreation decrease was due to less pool chemical usage and repairs; parks saw an increase in wages, and the auditorium increased as 2-sets of doors were replaced in 2012.
- Conservation & Development was a new category in 2010, the Zoning, Promoting and Advertising of Salem moved from General Governmental expenditures. The Planning and Zoning decreased largely due to the cost of updating the Zoning maps in 2011; and "Promoting & Advertising the City" decreased as the fire show was canceled in 2012. Total decrease was 48.6% or \$8,088.
- Miscellaneous Expenditures was back to zero in 2012. 2011 reported expenses for the buy-back of inventory from the operators of the Salem Bar.
- Water Fund Expenditures increased 3.1% - \$8,942. Chemical usage and filter usage increased in the WTP, but there were less water break repairs in 2012 (48% less \$7885) and wages decreased 9% directly due to this.
- Sewer Fund Expenditures increased \$1,324 - from repairs to the lagoon pumps.



SOURCE OF REVENUE (Figure A-4, A-5 and A-6)

Eighty-eight percent (88%) of the City's revenue is from taxes and charges for goods and services; with 39 cents of every dollar raised coming from charges for services (primarily water and sewer operations) and 49 cents of every dollar raised coming from some type of tax. (See Figure A-4). Another 9% is from state and federal grants for operating & capital purposes and the remaining revenue is from state-shared revenues and interest earnings. This varied slightly from 2011. Taxes saw a 1% increase (increase in sales & property taxes) and miscellaneous revenues decreased 4% (sale of the Salem bar building in 2011).

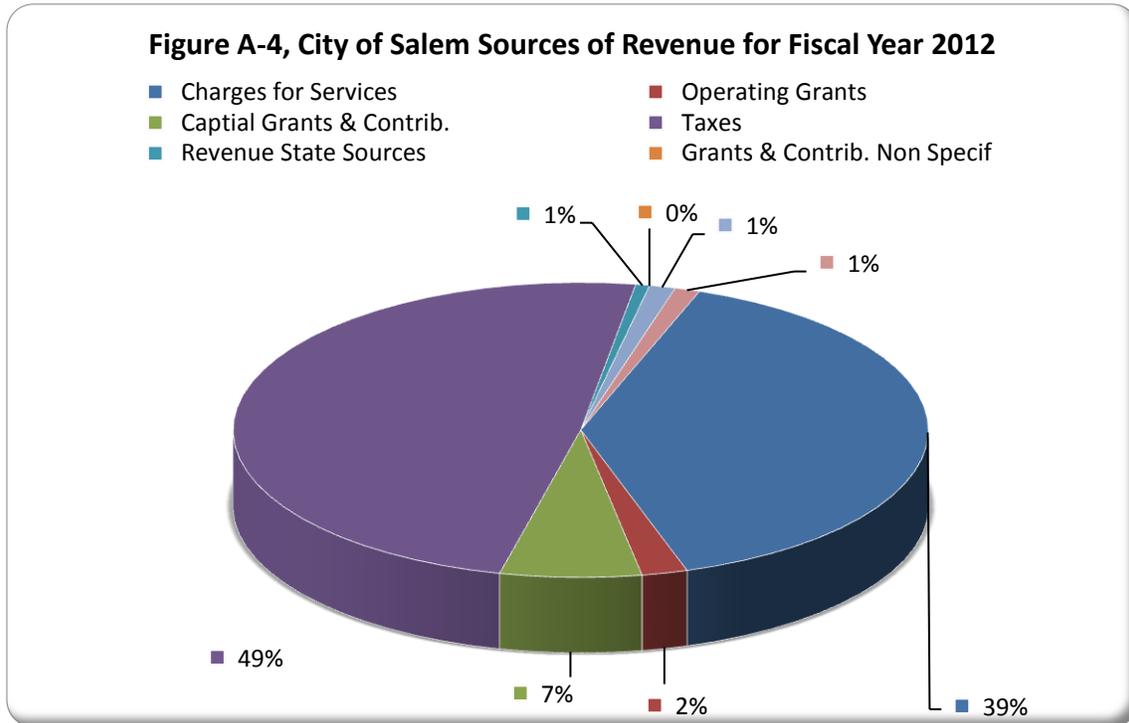


Figure A-5, City of Salem Sources of Revenue for Fiscal Year 2011

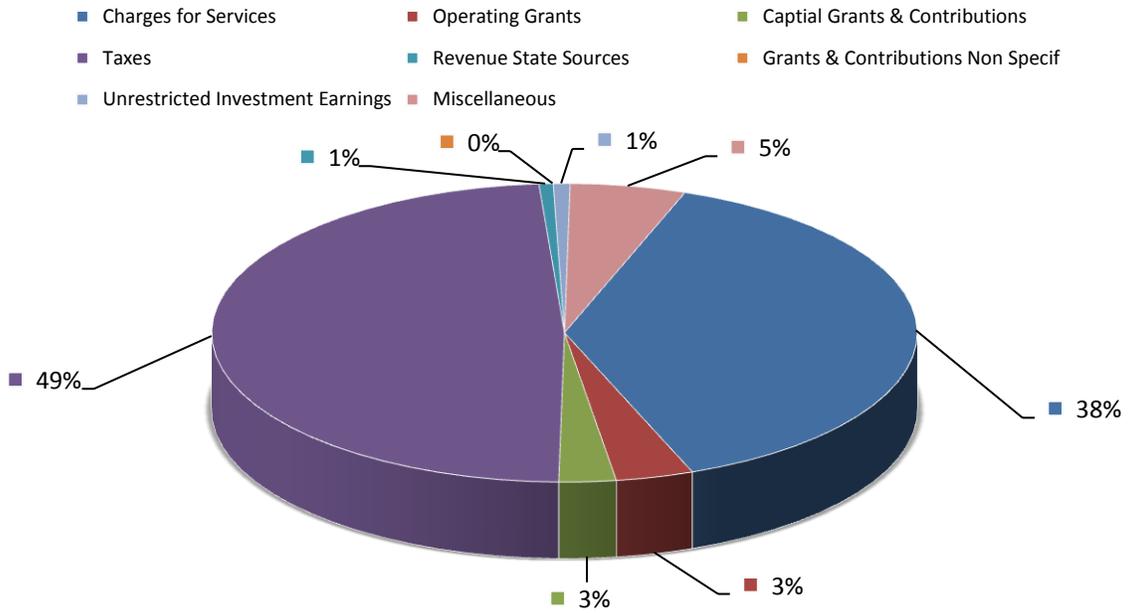
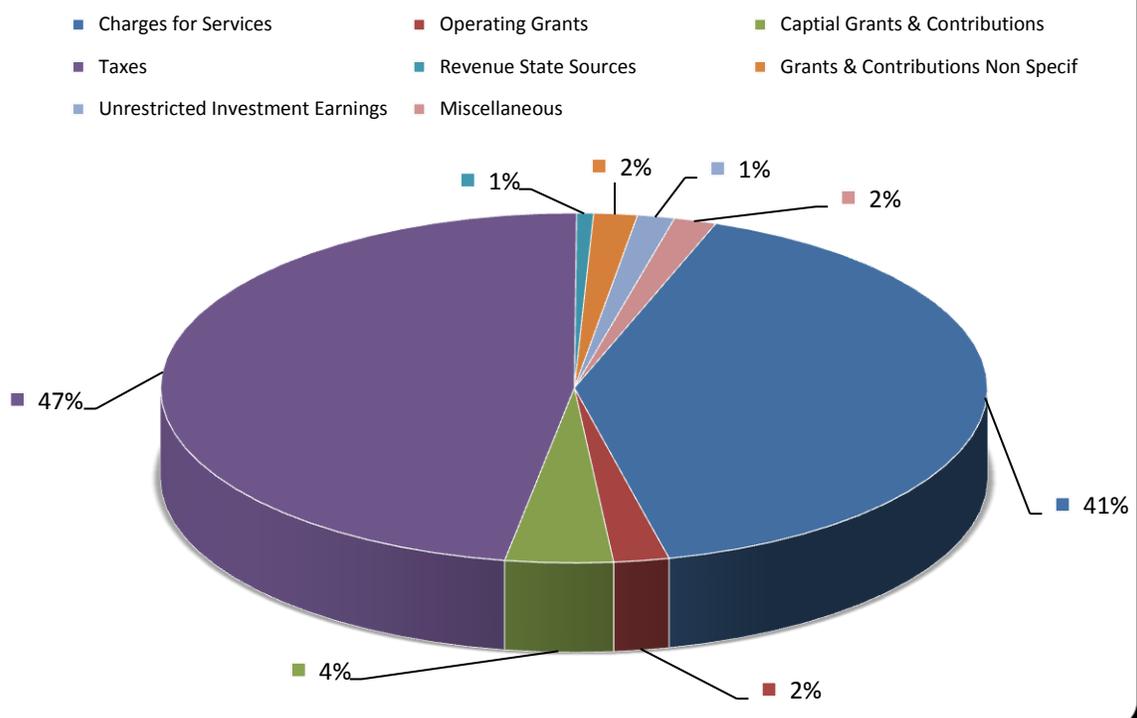


Figure A-6, City of Salem Sources of Revenue for Fiscal Year 2010



FUNCTIONAL EXPENSES - FIGURE A-7, A-8 and A-9

The City's expenses cover a range of services 61% related to public works services (road maintenance – chip seal – street sweeping – snow plowing; water & sewer system services). Culture and Recreation (Summer Recreation, Pool, Parks and Armory) make up 16%; General Government (Publications, Council, Attorney, Insurance, Finance Office & City Hall) accounted for 13%; Public Safety (Police, Civil Defense, and Fire Department) accounted for 9%; and Debt Service, Conservation & Development, Health & Welfare, and Miscellaneous expenditures each account for less than 1% of the 2012 expenditures. The expenditures service percentages varied slightly from 2011 – the difference between functions is mainly from the increase to public works for the 2012 road repair costs.

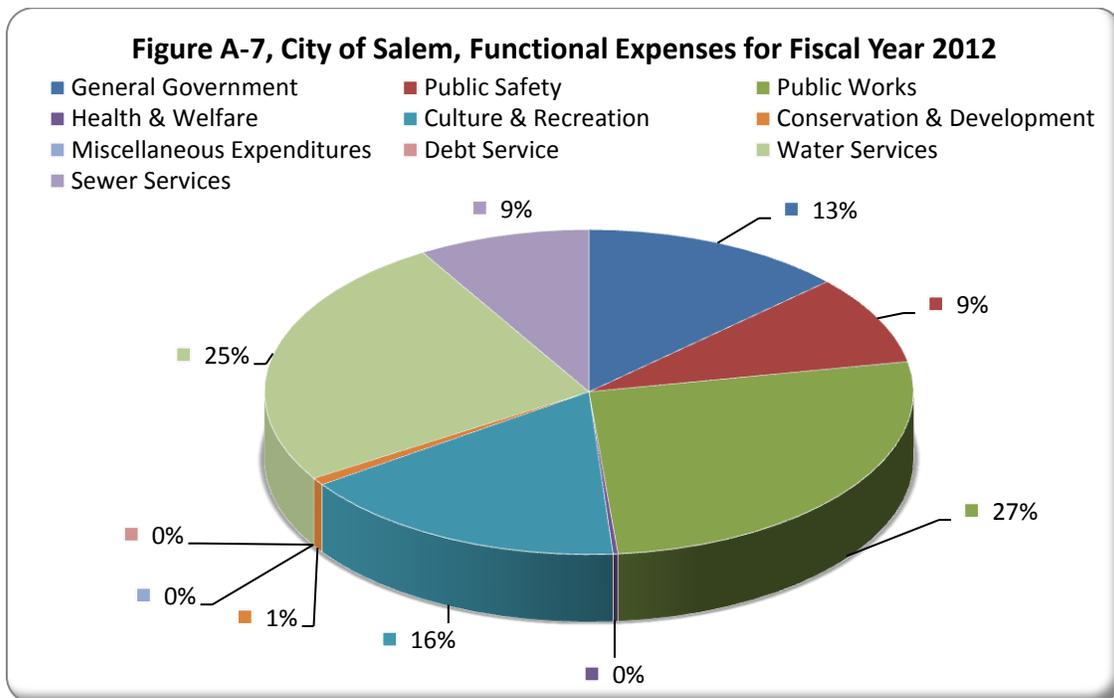


Figure A-8, City of Salem, Functional Expenses for Fiscal Year 2011

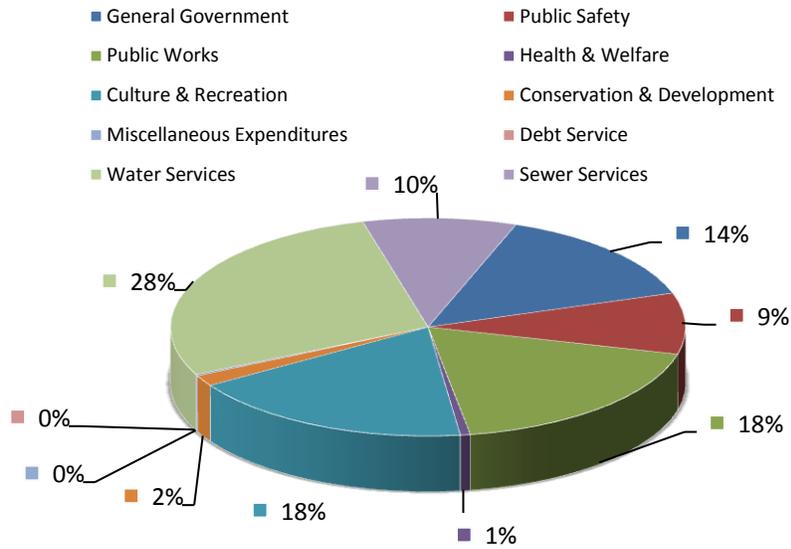
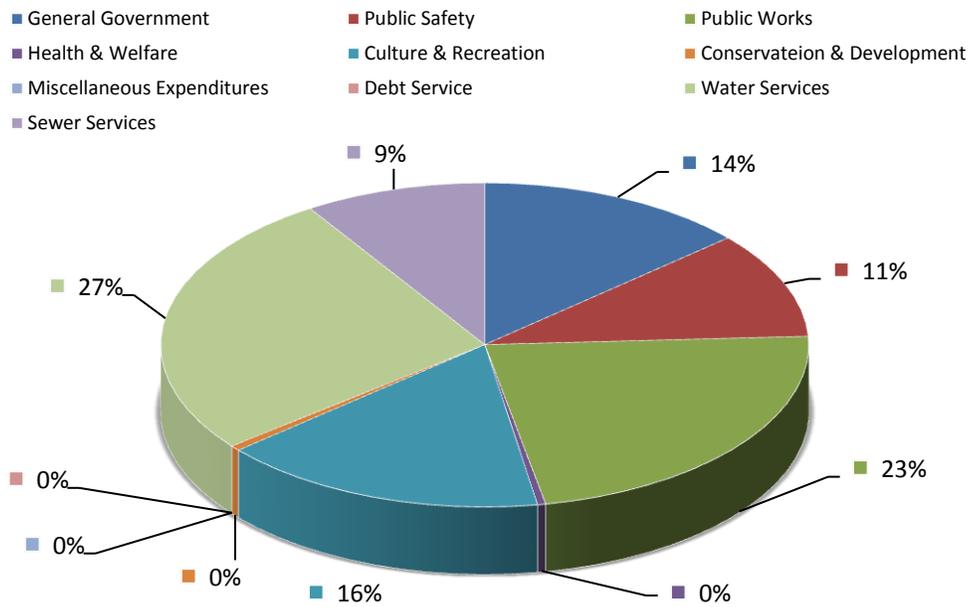


Figure A-9, City of Salem, Functional Expenses for Fiscal Year 2010



Governmental Activities

The City's Governmental activity revenues increased by 5.55%; both property tax & sales tax saw an increase; the Operating Grants, and Capital Grants & Contributions increased 49.6% - due to the donation of the building north of the armory; Investment Earnings increased 72.5%; and the Miscellaneous Revenue showed a decrease of 84.6% from the sale of the liquor store building in 2011.

The Governmental expenditures increased 21%. General Government expenses increased 3.9% due to a bi-annual audit in 2012; Public Safety costs increased 12.3% - the fire hall roof was replaced in 2012. The Public Works costs increased by 64.9% as \$99,734 more was spent on street patching, overlays & chip seal in 2012. Health & Welfare decreased 56% as less Mosquito Control chemicals were used in 2012. Culture & Rec increased 4.7% from the replacement of the south doors at the Armory. Conservation & Development decreased 48.6% in 2011 new zoning maps were purchased and in the 2012 fireworks show was cancelled due to dry weather. Miscellaneous Expenditures were zero as there was no buyback of inventory from the operating agreements; which was the case in 2011.

Business-type Activities

Operating revenues of the City's business-type activities increased 6.8%. The \$.60 increase to the water flat fee and \$.40 cent increase to the sewer fee; the amount of water produced and pumped into the system was 13.8% less than in 2011 and the water loss was at 10% in 2012 compared to 34.8% in 2011; which are all contributing factors to the operating revenue increase. The expenditures increased by \$10,265 (2.65%). The General Fund transferred \$37,092 (revenue from the sale of the liquor store building) to pay off the 2003 DW Loan; resulting in an increase to net assets of 6.1%.

- The Water Rates were adjusted in 2012 for the Filter Replacement and Equipment Repair and Replacement reserve accounts and operating expenses. The revenues generated from Charges for Services increased 11% (\$.60 Flat Fee increase) plus an increase in water usage paid (2011 saw a large water loss); the water surcharge fee collection and investment earnings also increased. The sewer department saw a 3.3% increase in revenues from user fees (\$.40 Flat Fee increase); investment earnings also increased in 2012.
- The increase in expenses was mainly from the Water Department. The Water Department's water treatment plant operating costs for filters and chemicals increased to what is now going to be the normal as the cleaning processes have been established and require more chemicals; the alternative to less cleanings is a reduction in the life of the filters. Wages decreased as there were less water main breaks. The sewer department's wages decreased but more dollars were spent on cleaning and televising the sewer mains and lagoon repairs.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The financial analysis of the City's funds mirror those highlighted in the analysis of governmental and business-type activities presented above. The City maintained five governmental funds - General, Sales Tax, Street Assessment, Storm Sewer and a Capital Projects Funds and only two business type funds - Water and Sewer Funds. Each fund other than the Sales Tax, Street Assessment & Capital Projects fund saw an increase in Net Assets.

General Fund Budgetary Highlights

Over the course of the year, the City Council revised the City's budget three times. These amendments fall into these categories:

- Supplemental appropriations and contingency transfers approved for unanticipated, yet necessary, expenses to provide for items necessary for the health and welfare of its citizens.

- Increases in appropriations, primarily by contingency transfer, to prevent budget overruns.

The three budget changes during the year were for the 2012 Street Project, cleaning of the storm drainage ditches, street repairs, the new restroom/concession stand building at the softball field, three radios for the fire department, street lighting utilities, and rubble site & park wages.

CAPITAL ASSET ADMINISTRATION

By the end of 2012, the City had invested \$5,879,449 in a broad range of capital assets, including, land, buildings, infrastructure, and various machinery and equipment. (See Table A-3.) This amount represents a net increase (including additions and deductions) of \$94,286 or 1.63% over FY2011.

TABLE A-3
CITY OF SALEM - CAPITAL ASSETS
(net of depreciation)

	Governmental			Business-type		
	Activities			Activities		
	2010	2011	2012	2010	2011	2012
Land	49,675	62,938	62,938	41,866	41,866	41,866
Buildings	173,908	155,018	197,532	1,246,661	1,220,688	1,194,716
Improvements Other Than Buildings	1,281,072	1,238,875	1,394,652	1,811,399	1,767,218	1,734,584
Machinery & Equipment	250,397	229,032	206,782	1,048,878	1,046,393	1,013,871
Construction In Progress	-	15,309	18,558	22,868	7,825	13,950
Total Capital Assets (Net)	1,755,052	1,701,172	1,880,462	4,171,672	4,083,991	3,998,987

This year's major capital asset additions include:

- The Governmental additions for 2012 are -
 1. Buildings increased for the donation of the cold storage building north of the armory.
 2. Improvements Other than Bldg increased from the rebuilding and matting of 2 streets - one petitioned and the other for repairs.
 3. Equipment shows a decrease for depreciation.
 4. CIP increased as the Softball field Concession Stand/Restroom expenses accrue.
- Business-type additions for 2012 are -
 1. Building decreased from depreciations.
 2. Improvements Other than Bldg decreased from depreciation being more than the cost of the Water Department's addition of a water main to the new building at the softball field, and the Sewer Department's refurbishing of four manholes and installation of a 2" forced sewer main for the new softball field building.
 3. Equipment decreased from depreciation
 4. The Construction in Progress dollars are from the purchase of Water Tower Telemetry Equipment but not installed.

The City's 2013 capital budget projects include the following: The Water Department plans on replacing two blocks of water main on Dakota St from Norton to Drake; the Sewer Department will be rehabilitating approximately four to five manholes. The Salem Youth and Recreation Boosters will finish building the concession stand/restroom building at the softball field complex with donations raised and volunteer labor. The Council will be designing and bidding out the replacement of the street lights on Main Street in 2013 – the project will include new wiring, poles and lights and will possibly be done in phases depending on the cost estimates. A major pool renovation project will be discussed, a grand stand at the baseball field complex will be replaced and the Council is pursuing a grant to install flashing speed signs on Hwy 81.

In 2012, the General Fund and Sales Tax Fund used \$196,279.32 in local cash for the 2012 Street Project, \$1807.90 for radius improvements, and \$12,919.21 for the building at the softball field complex (\$5,134.94 was the Summer Recreation Booster's share). The Water Department installed a water main to the new softball field complex building and purchased Water Tower Telemetry equipment with local cash of \$15,044.84. The Sewer Dept refurbished four manholes at a cost of \$8,750.00 and finished the 2" forced sewer main for the softball field complex concession/restroom building project – 2012 dollars spent were \$3252.56 and the total project cost was \$11,077.59.

The City had \$384,458.99 in the General Fund Capital Replacement Reserve Account at the end of 2012 – specifically for Main Street Lighting; baseball field fencing & improvements; Softball field complex Concession Stand/Restroom & playground equipment; Pool Bathhouse/Improvements; Armory Door Replacement and Street projects. The 2013 Budget placed an additional \$147,861 into the Capital Reserve Account – specifically for Street Projects; Main Street Lighting; Pool Renovation and sidewalk projects. The City will continue to put block(s) of water main in as money is available.

LONG-TERM DEBT

At year-end, the City had \$2,058,575 in SRF Loans (Revenue Bonds), and \$19,105 in other long-term obligations. This is a decrease of 9% as shown on Table A-4 below. The City's obligation for compensated absences increased 15.5% (as the vacation hours carried over into 2013 increased), and the SRF loan balances decreased \$205,762 from the payments made on debt (the 2003 DWSRF loan was paid off in 2012).

TABLE A-4
CITY OF SALEM - Outstanding Debt and Obligations

	Governmental			Business-type		
	Activities			Activities		
	2010	2011	2012	2010	2011	2012
Compensated Absences	11,710	11,138	13,118	4,210	5,400	5,987
Drinking Water SRF Loan 2003	-			49,352	36,815	-
Drinking Water SRF Loan 2005	-	-	-	285,626	272,314	244,362
Drinking Water SRF Loan 2008	-	-	-	1,304,217	1,275,906	1,216,462
Clean Water SRF Loan 2003	-	-	-	392,933	370,265	322,489
Clean Water SRF Loan 2005	-	-	-	325,121	309,036	275,262
Total Outstanding Debt Obligations	11,710	11,138	13,118	2,361,458	2,269,737	2,064,562

The City is liable for the accrued vacation leave payable to all full-time and permanent part-time employees who have been employed for more than one year. The up and down between the Governmental Activities and Business Type activities is due to the varying time worked in the funds from year to year and the amount of hours carried over annually (1 week is allowed to be carried over).

The City has outstanding \$1,460,824 in Drinking Water SRF Loans and \$597,751 in Clean Water SRF Loans (Revenue Bonds). The bonds are secured and paid for from the Water and Sewer Funds. The City does not anticipate the use of any tax dollars to pay for these bonds.

- The 2003 bonds were used for the 2003 Street and Utility Project (This project extended water and sewer service on S. Main Street and on Brown Ave; and started the Storm Sewer System in Southeast Salem.) The 2003 DWSRF Loan was fully paid off on January 9, 2012, two and one half years earlier than the scheduled date of July 15, 2014 and the 2003 CWSRF will be fully paid off on July 15, 2024.
- The 2005 bonds were used for the 2005 Street and Utility Project (This project replaced Water main on Nebraska and Essex Streets; extended storm sewer on George Ave and replaced storm sewer on Essex Ave.) The 2005 CW SRF Loan closed in 2006 and the DWSRF Loan closed in 2007. Both are 20 year loans – the CWSRF will be paid off in July 2026, and the DWSRF will be paid off in April 2027.
- The 2008 DWSRF Loan closed in 2009, this is a 30 year loan and will be paid off in 4/15/2039. The loan is specifically for the Water Filtration (Treatment) project, and a Water Surcharge was established to pay off the debt on this bond. Each household pays \$9.90 per month or 118.80 annually to retire the debt.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's current economic position has increased annually from a slight decline in 2008. The City experienced growth of 1.4% in 2012; 1.3% in 2011 and 1% in 2010. The growth factor gives the City the ability to increase the amount of revenue generated from property taxes, the increase for 2013 is \$3,886.69; in 2012 it was \$3,490.59; and in 2011 it was \$2,660. Under the state mandated property tax freeze, property taxes from one year to the next may increase 3% or an amount based on the Consumer Price Index (CPI) whichever is lower plus the growth factor. 2012 property tax levy requests payable in 2013 increased 4.4% (Growth 1.4%; CPI 3%) - \$12,215; up from 2011 property tax levy requests payable in 2012 which increased 3.4% (Growth 1.3%; CPI 2.1%) or \$9,129.; 2010 property tax levy requests payable in 2011 only increased 1% (Growth 1%; CPI 0%) or \$2,660.00.

One of the primary sources of revenue for the City is taxable retail sales in the community (sales tax). In studying the actual sales tax revenue received (once revenue was received for the entire FY), the 2012 vs. 2011 taxable sales base increased 4.41% (\$999,150.50) and the 2012 vs. 2010 taxable sales base increased 22.39% (4,322,849). The City's 2013 tax revenue budget was increased 8.4%.

The City passed an Ordinance in 2007 implementing an additional 1% tax on gross receipts from the sale of leases or rentals of hotel, motel, campsites or other lodging accommodations; the sale of alcoholic beverages as defined in SDCL 35-1-1; establishments where the public is invited to eat, dine or purchase and carry out prepared food for immediate consumption; and ticket sales or admissions to places of amusement, athletic and cultural events within the municipality. The tax was not payable until January 2008 and was estimated to generate \$11,000.00 in revenue; this revenue can only be used for the purpose of land acquisition, architectural fees, construction costs, payment for civic center, auditoriums or athletic facility buildings, including the maintenance, staffing and operations of such facilities, and the promotion and advertising of the municipality, its facilities, attractions and activities. The actual dollars raised by this tax in 2012 was \$20,538.96 a decline of 4.47% from FY2011; 2011 receipts were \$21,499.57 a decline of 12.22% from FY2010; in 2010 the taxes collected were \$24,491.42 a 72.58% increase from 2009. The 2010 increase is thought to be from audits performed by the Dept of Revenue; it appears that some businesses were not paying the tax. The City's 2013 budget does have an appropriation for Economic Development - a contract with SEPF through the Greater McCook Development Alliance. The fund was also used in 2012 to fund a portion of the 2012 Street project and is considered as a means of finance for projects. The revenues are in a "Special Revenue Fund" as designated by SDCL 10-45.

The City's adopted 2013 General Fund budget decreased 21% to \$959,686. The City's General Government Budget decreased 3.6; decrease of \$4,000 to the Contingency; and an Administrative Department decrease of \$5,980.00 (decrease for 2012 Audit and increase for computer replacement/training). There was a decrease in Public Safety as the repairs to the fire hall roof were part of the 2012 budget; Public Works increased \$65,535 as additional money was allocated for the purchase of a new maintainer and street lighting utilities; Culture and Recreation decreased as the softball field concession stand/restroom building was supposed to be completed in 2012; and the 2-sets of doors at the Salem National Guard Armory building were installed in 2012; Capital Outlay remained the same and Capital Replacement decreased by \$63,139. The remaining departments varied slightly to accommodate a shift in wages between departments. The 2013 budget was increased to accommodate a raise for the city's employees (4% full-time & 2% part-time); wages are not set until January.

The City's business-type activities (water and sewer operations) expect that the revenues for the 2013 financials will increase as a consequence of a \$0.30 cent Water flat fee and \$0.60 cent Sewer flat fee rate increase. The flat fees were increased for filter replacement in the Water Treatment Plant and water main replacement; and in the Sewer Department to partially adjust to the new regulatory fee of \$22.00. The 2013 Water Operating Budget increased 2.4% (\$6,173) from 2012 and the 2013 Sewer Budget increased 2.4%.

The Council increased the Water Flat Fee \$.30 but provides a \$3.00 reduction to those living alone on social security with no other retirement income. Those residents qualifying are required to file an affidavit claiming they meet the qualifications for the reduced rate with City Hall. The 2013 rates are a water flat fee of \$13.40, .004 cents per gallon used, plus a \$9.90 Water Surcharge fee. The Sewer Rates increased by .60 cents to a Residential flat fee of \$21.00, and 40% of the Water Usage Fee but not less than \$21.00 for commercial users. A CIP increase to the water rate was projected; the need to replace 30 blocks of 4" CIP water main and filters in the Water Treatment Plant required a minimum of the 3% CPI. (.30 cents is a 3.05% increase). At the end of 2012, the Equipment Repair & Replacement Fund had a balance of \$125,716.29; a 37.77% increase; a direct result of the rate increases in 2011 & 2012. This fund is necessary for the replacement of water main and the Nano & Ultra Filters at their scheduled life expectancies, and to meet the 110% Debt obligation on the DWSRF loans. The \$.30 cent increase was necessary to increase the dollars for water main replacement. The water department allocated \$33,600 to the filter reserve and \$16,000 to water main replacement in 2012 and in 2013 is projected to allocate \$16,500 to the filter reserve and \$31,000 to the water main reserve both designated in the Equipment Repair/Replacement Fund. The Sewer Department rates were increased by .60 cents (2.9%) and will be increased annually to eventually reach the \$22.00 State rate for 5,000 gallons. All rates are reviewed annually. The water & sewer customers saw a .90 cent increase to their monthly bill; or \$10.80 annually.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Salem's Finance Office, 400 N. Main, P.O. Box 249, Salem, SD 57058.